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IN THE

Supreme Court of the United States

October Term, 1975
No. 75-596

HOWARD BERSCH,

Petitioner,

v.

ARTHUR ANDERSEN & CO., I.O.S., LTD., and BERNARD CORNFELD,

Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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IN THE

SUPREME COURT OF THE UNITED STATES

October Term, 1975

No._____

Howard Bersch,

Petitioner,

-against-

Arthur Andersen & Co., I.O.S., Ltd., and Bernard Cornfeld,

Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

Petitioner prays that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Second Circuit, entered on April 28, 1975.

OPINIONS BELOW

The opinion of the United States District Court for the Southern District of

New York (Hon. Robert L. Carter), determining,on defendants' motions to dismiss, that the Court had subject matter jurisdiction under the Securities Act of 1933, 15 USC §§77a et seq. and the Securities Exchange Act of 1934, 14 USC §§78a et seq., that the Court had personal jurisdiction over all defendants except J. H. Crang & Co. and certifying the question of subject matter jurisdiction pursuant to 28 USC §1292, was filed on December 4, 1974 and is reported at 389 F. Supp. 446 (S.D.N.Y. 1974). The opinion is printed as Appendix "A" to this Petition.

The opinion of the United States Court of Appeals for the Second Circuit, reversing the determination of subject matter jurisdiction with respect to all class members except American citizens and residents and remanding, and affirming the judgment dismissing the complaint as against defendant

J. H. Crang & Co. on grounds of lack of personal jurisdiction, was rendered on April 28, 1975 and is reported at 519 F. 2d 974 (2d Cir. 1975). The opinion is printed as Appendix "B" to this Petition.

JURISDICTION

The judgment of the Court of Appeals was entered on April 28, 1975. A timely petition for rehearing was denied by the Court of Appeals on July 23, 1975. The order is printed as Appendix "C" to this Petition. This Petition is being filed within ninety days after the entry of the aforesaid order denying reargument. Jurisdiction is conferred on this Court by 28 USC §1254(1).

QUESTION PRESENTED

Did the Court of Appeals, in determining the issue of subject matter jurisdiction under the Securities Act of 1933 and the Securities Exchange Act of 1934, adopt a discriminatory and dangerous interpreta-

tion of those statutes,in conflict with the language of the statutes, the purpose impelling their enactment, the principles of international law and decisions of this Court, when it held that in connection with claims arising out of an allegedly fraudulent offering of securities,the district court lacks subject matter jurisdiction with respect to the claims of non-resident aliens, even though it has subject matter jurisdiction with respect to the identical claims of alien residents or citizens resident at home or abroad.

STATUTES INVOLVED

The statutes involved are: §§12, 15 and 17 of the Securities Act, 15 USC §§77l, 77o and 77q,and §§10 b, 15(c)(1), 20 and 30 of the Securities Exchange Act, 15 USC §§78j(b), 78o, 78t and 78dd . They are reprinted as Appendix "E" to this Petition.

STATEMENT OF THE CASE

This action was commenced as a class action in December, 1971, on behalf of all persons who purchased common stock of IOS, Ltd. (IOS) at a public offering of such stock made on or about September 24, 1969 (Public Offering)*. The complaint alleged that the prospectus pursuant to which the Public Offering was made was false and misleading in that it failed to reveal material facts concerning IOS' finances, illegal activities, chaotic bookkeeping, mismanagement and actual looting and plundering

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* The Public Offering consisted of a primary offering of 5,360,000 shares sold by IOS and a secondary offering of 5,392,000 shares sold by 490 IOS shareholders. The primary offering was managed by defendant Drexel Firestone, Inc.(Drexel); the secondary offering was managed by defendant J. H. Crang & Co. (Crang) and Investors Overseas Bank Limited (IOB). Three substantially identical prospectuses were used in connection with the Public Offering.

of IOS's treasury. Plaintiff and the class, based upon the prospectus, paid $110 million for IOS stock. Shortly after the Public Offering, the stock was worthless. Plaintiff (Petitioner) contends that if all material facts had been disclosed, the class would have known that the stock had no value and would not have purchased it.

The two leading underwriters of the primary offering were American firms, Drexel and Smith, Barney & Co., (Smith Barney) with headquarters in the United States. Both are broker-dealers, registered with the Securities and Exchange Commission (SEC). These firms, in the United States, made or participated in the making of many judgments which not only influenced but structured the entire underwriting, including the quality of disclosure. Such decisions included the determination of:

1. The size of the offering.

2. The price of the offering.

3. The firms to be invited to participate in the offering.

4. Commissions to be paid.

5. The time schedule of the offering.

6. The contents of the prospectus.

7. The adequacy of the financial statements.

8. The accuracy of the prospectus.

The participation of United States underwriters was essential to the success of the IOS Public Offering. These underwriters lent their prestige and capital to the offering and augmented its American image. The ensuing debacle directly affected the American underwriters who, as testified to by the President of Drexel, lost foreign business and, additionally, affected the integrity of the United States securities markets since American firms were so heavily implicated.

In addition to the underwriters, other American firms played major roles in the underwriting. The accounting firm of Price Waterhouse was retained by Drexel as a consultant to study and report on IOS and that firm performed significant work here. The American accounting firm of Arthur Andersen & Co. played a paramount role in the offering, placing its imprimatur upon the false financial statements contained in the prospectus.

The attorneys for the American underwriters and the issuer were also American. The New York firm of Shearman & Sterling was retained by Drexel as counsel to advise it in connection with the underwriting and, in particular, the preparation of the prospectus. Another New York law firm, Willkie, Farr & Gallagher, participated as counsel for the issuer. In addition, Stammer & Haft, New York attorneys for IOS in connection with certain matters, were consulted

with reference to the contents of the prospectus, and Edward Cowett (Cowett), a New York attorney and executive officer of IOS, was also active in the preparation of the prospectus, as well as most other aspects of the entire project.

Many key decisions were made in the United States. Drexel conducted a preliminary investigation of IOS, consulted counsel and held an exploratory meeting with the SEC here. On the basis of those efforts, which were thoroughly discussed and analyzed on a top executive level, in New York and Philadelphia, it determined to undertake the IOS underwriting.

The lead underwriters negotiated the price of the issue for the entire offering and the amount of the underwriting concession. These negotiations took place to a large extent in New York, where Bertram Coleman (Coleman), Chairman of the Board of Drexel, and Cowett of IOS agreed upon

a pricing formula and conducted a preliminary discussion on underwriting commissions. Additionally, allocation of shares to members of the syndicate was made by the underwriters in New York.

Essential to the preparation of a prospectus is a due diligence investigation of the issuer by the underwriters. A significant part of the due diligence investigation in this case took place in New York. Meetings were held in New York with attorneys for IOS and meetings were held with the SEC in an attempt to gain information about the issuer. In addition, Price Waterhouse was retained in New York to study and report on IOS. Its report was prepared, distributed and discussed in New York. That report was of extreme importance since the most significant effort to comply with due diligence was made by Price Waterhouse. That firm and, in particular, Frederic Werblow (Werblow),

the partner in charge, spent considerable effort in a review of IOS's financial operations and the proposed descriptions of those operations contained in the prospectus. The evidence indicates that approximately 50% of Werblow's work was performed in the United States. Werblow testified that he received his instructions in New York, and held meetings there with officials of IOS, Arthur Andersen and Drexel. After Price Waterhouse completed its work, an all-day meeting lasting into the evening was held in New York to discuss the IOS Public Offering. The participants reviewed and discussed all IOS financial statements. Other meetings were held in New York to report on Price Waterhouse's progress, with Andersen present and participating therein. Price Waterhouse rendered reports to Drexel laying bare the true state of IOS' operations; the reports were prepared in New York and discussed there. Those reports made known gross de-

ficiencies in the prospectus and affirmatively demonstrate that Andersen was made aware in New York of the fraudulent nature of the Public Offering.

Although much of the prospectus was drafted in Europe, certain significant parts were written in New York. These include a sticker affixed to the cover of the prospectus which referred to a proceeding brought against IOS by the SEC. Other documents prepared in New York pertain to dealings with United States companies and IOS's real estate activities in Florida.

Grayson M. P. Murphy (Murphy), a member of Shearman & Sterling, was in charge of the work to be performed by his firm.The evidence reflects that a substantial amount of Murphy's time and effort devoted to the underwriting and particularly to the prospectus, involved New York activities.

Drexel's board and executive committee, meeting either in New York or Philadelphia, were kept informed of the progress of the offering,and Murphy regularly reported directly to them.

In all the aforesaid transactions, the facilities of interstate commerce were continuously employed and the record is replete with evidence of constant international communication by virtually every conceivable form, including telephone, mail, airplane and telex.

An investigation of IOS's Florida real estate operations was made in the United States at the request of Drexel. A written report thereon was submitted to the underwriter in Philadelphia.

Publicity for the proposed offering was released in New York in violation of the antifraud provisions of the federal securities laws. During the months pre-

ceding the IOS Public Offering, defendant Cornfeld and other IOS officials touted the company's prospects in American media, such as Newsweek magazine.

American were both purchasers and sellers in the Public Offering. Bernard Cornfeld and other Americans were the principal sellers in the secondary offering. The record reflects that some 360 Americans purchased at the Public Offering. Plaintiff Bersch read all three prospectuses in New York and made his purchase here.

The closing statement for the underwriting was drafted in New York, printed in New York and distributed therefrom. All participants were directed to make payments for the stock in New York in United States dollars to "Bank of New York, 8th Floor, 20 Broad Street, New York, New York 10015."

Thus, the offering began, progressed and ended here. Although many of the tech-

nical and administrative aspects of the offering took place abroad, in the final analysis, it was directed from the United States. All of the Americans directly or indirectly involved in effecting the fraudulent enterprise profited from it - the selling stockholders, the underwriters, and the professionals, accountants and lawyers.

On defendants' motions to dismiss, the District Court found that it had subject matter jurisdiction over all claims. It determined that the primary underwriting headed by Drexel and Smith, Barney and the secondary offering headed by Crang and IOB were, in essence, one offering for purposes of subject matter jurisdiction. Further, it held, the level of activity by United States citizens within the United States in connection with that offering was of such significance, combined with some negative impact on the American market, to warrant the exercise of subject matter jurisdiction over all class

members' claims.*

The District Court, pursuant to §1292 (b), certified the issue of subject matter jurisdiction for interlocutory appeal purposes, and the Court of Appeals agreed to take the appeal.**

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* It also held that it lacked personal jurisdiction over Crang, that the manner of service and delay in service on IOS and Cornfeld did not warrant dismissal as against them and that it should not stay the action pending the winding up of IOS by Canadian authorities.

** At about the same time, defendants Andersen, Cornfeld and IOS filed appeals from a December 4, 1974 order by the District Court directing that notice be sent class members of a hearing on a partial settlement reached with defendants Drexel, Smith, Barney, Banque Rothschild, Hill Samuel, Guinness Mahon and Pierson, Heldring & Pierson, contending that such order was a determination of class action status and hence appealable under the Second Circuit's decision in Herbst v. International Telephone and Telegraph Corporation, 495 F. 2d 1308 (2d Cir. 1974) and this Court's decision in Eisen v. Carlisle & Jacquelin, 417 U.S. 156 (1974).

Defendants Andersen, Cornfeld and IOS moved to consolidate their appeals from the December 4 order with the instant appeals, and their motions were denied on January 29, 1975.

The Court of Appeals reversed the District Court's order insofar as it sustained subject matter jurisdiction with respect to

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[footnote continued]

Furthermore, the Court of Appeals denied defendant Andersen's motion for permission to file an outsized brief in the instant appeal on February 3, 1975. Defendant Andersen had sought to file an outsized brief in an effort to challenge the constitutionality of Rule 23 of the Federal Rules of Civil Procedure.

Despite these two indications from the Court of Appeals that it would determine the issue of subject matter jurisdiction separately from the class action issue, that court, clearly ignoring its prior actions, based its decision herein entirely on the class action aspects of the case and chided plaintiff for not coming to grips with that issue.

The class action appeal, having been effectively mooted by the Court of Appeals decision on the subject matter jurisdiction appeal, has been stayed.

all purchasers of IOS securities and affirmed it insofar as it sustained such jurisdiction with respect to purchasers who were American residents or citizens. The Court remanded the cause for modification and further consideration of the class action determination in light of its opinion.*

This Petition for Certiorari is filed in connection with defendants Arthur Andersen, IOS and Cornfeld, only.

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* The Court of Appeals also affirmed the District Court's order dismissing the complaint as against Crang for lack of personal jurisdiction and denied petitions for mandeamus by IOS and Cornfeld with respect to the manner of and delay in service of process and without prejudice, with respect to IOS' application for a stay.

REASONS FOR GRANTING THE WRIT

I.

THE EXTRATERRITORIAL REACH OF THE FEDERAL SECURITIES LAWS IS NOW A MATTER OF CONJECTURE. THIS COURT SHOULD CONSIDER THE SCOPE OF THOSE STATUTES.

The instant appeal presents important and as yet unresolved questions with respect to the extra-territorial scope of the federal securities laws. The Securities Act and the Securities Exchange Act were enacted in 1933 and 1934, respectively, many years prior to the tremendous growth of the mutual fund industry, the phenomenon of the offshore fund, the development of the large multi-national corporation and the increasing internationalization of the securities markets. Those who drafted the federal securities laws did not contemplate the complexity of modern international securities transactions and, as a result, the securities statutes fail to define their extraterritorial

reach. Accordingly, in the absence of express legislative direction, it has become the province of the courts to fill in the interstices of regulation.

The process of judicial interpretation, however, has been slow, and the results have been scant. Although the courts have valiantly sought to define the limits of the extraterritorial application of the antitrust laws for more than half a century, there has been little effort expended in a corresponding attempt to clarify the scope of the federal securities laws. Indeed, the first case to consider the extraterritorial application of the Securities Exchange Act was decided in 1960, more than 25 years after its enactment.*

There has been a dearth of judicial interpretation of the extraterritorial application of the securities laws, despite the marked increase in the number and complexity

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*Kook v. Crang, 182 F. Supp. 388 (S.D.N.Y. 1960).

of international securities transactions involving American contacts and interests. Indeed, prior to the instant case, only two major decisions, Schoenbaum v. Firstbrook* and Leasco Data Processing Equipment Corp. v. Maxwell,** have shed significant light upon the jurisdictional requisites for the extra-territorial application of the securities laws and in particular, their anti-fraud provisions. These decisions, however, have raised more questions than they have solved. Additionally, as discussed more fully below, in both Leasco and the instant case, the Congressional design with respect to jurisdiction has been divined, if not created, by a judge who,petitioner submits, articulated, not the legislative intent, but, rather, his

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*405 F.2d 200 (2d Cir. 1968), reversed on other grounds, 405 F.2d 215 (2d Cir. 1968) (en banc), cert. denied, sub. nom Manley v. Schoenbaum, 395 U.S. 906 (1969).

**468 F.2d 1326 (2d Cir. 1972)

own subjective perception of the "good and true."*

The within petition involves jurisdictional issues with which this Court has not directly dealt in the context of the federal securities laws. The cases decided by this Court and relied upon by the Court of Appeals dealt with jurisdictional problems arising in connection with the extraterritorial application of entirely different legislation. Thus, Steele v. Bulova Watch Co.** arose under the Lanham Act and United States v. Aluminum Co. of America,*** the antitrust laws. Although those statutes may invite some comparison with the federal securities laws, the underlying policies, as well as the nature of the problems involved, present

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*Hand, The Spirit of Liberty, (2d Ed. 1954), p.156.

**344 U.S. 280 (1952)

***148 F.2d 416 (2d Cir. 1945).

different considerations in any determination of extraterritorial reach.*

Further, the courts are in disagreement as to whether the principles espoused in the antitrust cases are applicable to the securities laws and, if so, to what extent. Thus, although the courts and commentators agree that in antitrust cases, jurisdiction may properly be based upon the presence of deleterious effects on commerce, the cases are in disagreement as to whether effect within the jurisdiction is, in and of itself sufficient to warrant the exercise of juris-

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*For example, the Lanham Act is designed to protect the individual trademark owner, whereas the securities laws are designed to protect the integrity of the United States securities markets and preserve them as a principal means of providing private investment capital for the United States economy. Although a similar purpose imbues the federal antitrust laws, i.e., the preservation and protection of the structure of the American economy, they present somewhat different problems in the international sphere, in light of differing foreign attitudes towards monopoly. Indeed, the case would appear stronger for extraterritorial application of the Securities Exchange Act than the Sherman Act, since fraud is universally proscribed, whereas foreign reaction

diction for violation of the securities laws. The Second Circuit in Schoenbaum held that federal jurisdiction did encompass a totally foreign transaction which affected stock registered on an exchange within the United States. In Leasco, however, the Second Circuit held that "despite United States v. Aluminum Co. of America... and Schoenbaum," it entertained "most serious doubt" whether, absent misrepresentation in this country, Section 10b would be applicable simply because fraud in the purchase of the securities affected an American corporation whose stock was listed on the New York Stock Exchange and its shareholders. In Travis v. Anthes Imperial, Ltd.,* on the other hand, the Eighth Circuit was "persuaded" that Section 10b would be applicable, even if it were assumed that all the fraudulent dealings took place in Canada, since the conduct outside the

(footnote continued)

to cartels is not uniform and has even included active encouragement of their use as instruments of foreign policy. See, Hexner, International Cartels, (1946).

*473 F.2d 515 (8th Cir. 1973)

country resulted in diminution in the value of stock held by plaintiffs in a Canadian corporation not listed on any American stock exchange. The court relied upon United States v. Aluminum Co. of America, Ohio v. Wyandotte Chemical Corp.* and Section 18 of the Restatement (2d) of the Foreign Relations Law of the United States.

The most extreme position with respect to the extraterritorial application of the securities laws has been taken by the SEC, the agency entrusted with their construction, implementation, and enforcement.** That agency has consistently argued, without judicial support,*** that the use of the facilities of inter-

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*401 U.S. 493, 500-501 (1971)

**"When faced with a problem of statutory construction, this Court shows great deference to the interpretaton given the statute by the officers or agencies charged with its administration", Udall v. Tallman, 380 U.S.13, 17 (1965).

***Although the Court in Leasco considered

state commerce is, in and of itself, sufficient to warrant application of the federal securities laws to a foreign transaction. That argument is based upon the theory that the United States has a direct interest in the use to which the facilities of interstate commerce are put and that any fraudulent use of such facilities warrants extraterritorial application.*

Thus, it is apparent that the law in this area is both unsettled and confused. Petitioner believes that it is of supreme importance that this Court express its views on the issue of the extraterritorial reach of the federal securities laws. In recent years, international securities trading has increased phenomenally. United States citizens invest large sums in foreign

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(footnote continued)

the use of the facilities of interstate commerce to constitute conduct within the United States, it did not agree that such use, however incidential, would warrant the exercise of jurisdiction.

*See SEC v. United Financial Group, Inc. 474 F.2d 354 (9th Cir. 1973).

securities,and foreigners invest in American securities markets, particularly through the medium of large foreign-based mutual funds. Additionally, it is anticipated that such transactions will proliferate as the world moves toward a common market in securities. The barrier of distance which served to confine securities transactions to a single country no longer exist,and some degree of diversification is now accepted by investors. Today, sophisticated communications systems and computers, combined with such factors as the stabilization of the foreign exchange markets, have enabled investors throughout the world to trade on and invest in numerous foreign markets with a high degree of speed and ease.

In disputes arising from international securities transactions, litigants of all nationalities must depend upon national courts to adjudicate controversies involving international facts. Petitioner submits that the United States has a peculiar responsibility of leadership because of its

paramount position in the world's securities markets to formulate acceptable standards of conduct in securities transactions involving Americans and affecting American interests. A decision by this Court defining the reach of the federal securities laws would go far toward putting "on notice" both Americans and foreigners engaged in international securities transactions as to what conduct and circumstances American courts will deem sufficient to warrant the exercise of jurisdiction.*

II

THE DECISION OF THE COURT OF APPEALS WAS ERRONEOUS AND WILL HAVE SERIOUS CONSEQUENCES, UNDERMINING THE EFFECTIVENESS OF THE FEDERAL SECURITIES LAWS IN THIS AGE OF INCREASING TRANSNATIONAL ACTIVITY.

The instant petition presents for review important issues with respect to the

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*Subjecting an offender to rules that are uncertain raises a question of due process--fairness.

extraterritorial reach of the federal securities laws. The case derived from an international securities transaction, massive in size, complex in concept and execution, involving all of the various factors previously deemed critical in the jurisdictional calculus. In a simplistic opinion, fundamentally based upon a concern with nationality and an antipathy toward class actions, the Court of Appeals determined that while under recognized principles of international law, Congress could have empowered the District Court to exercise jurisdiction, Congress would not have wished to do so.

Although the Court of Appeals assertedly sought to determine "what Congress would have wished," it "freely acknowledged that if [it] were to point to the language in the statutes, or even in the legislative history, that compelled [its] conclusions, [it] would be unable to respond." Thus, as the Court

stated, its determination of Congressional intent rested upon case law, commentary and its "own best judgment." In the adjudicative mix, petitioner contends, the latter was the primary ingredient.

While it may well be true that Congress did not "foresee the development of off-shore funds" at the time the federal securities laws were enacted, it does not follow that the statutes, themselves, are unhelpful in determining Congressional intent. In reaching its decision, however, the Court of Appeals ignored the principles of sound statutory interpretation and premised its opinion primarily upon the prejudices of its author with respect to class actions. The conclusions of the court are unsupported by statutory language, run counter to the very fabric of the securities laws, and, petitioner submits, if allowed to stand will constitute erroneous and dangerous precedent.

A. The Court Did Not Truly Seek the Congressional Intent, But Rather, Substituted its Own View as to What Such Intent Should Have Been

> "In construing a statute whose meaning is not clear, the first inquiry is one as to legislative intent, pursuant to the obligation of giving effect to the plain purpose of the statute ... Legislative intent has no reference to what may have been in the mind of the person who wrote the statute, or whether there was anything in particular in the minds of individual legislators who voted for its enactment. Intent as here used relates to the purpose to be served by the statute, and the statute is to be looked upon as if some unified legislative spirit motivated its enactment."*

To discover this mind or spirit in the absence of clear legislative history, resort should be had to an examination of the conditions comprising the background of legislative action and the language of the statute itself. Thus, the statutory language and legislative purpose are the principal determinants in a search for Congressional intent.

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*Day v. North American Rayon Corp., 140 F. Supp. 490, 491 (W.D. Tenn. 1956) (citations omitted)

The mere fact that Congress did not anticipate the tremendous changes in the milieu of securities transactions does not vest the court with unbridled authority to guess what the legislative "would have intended on a point not present to its mind, if the point had been present."* As one commentator has noted, "what a legislator did think of makes a difference. But what he did not think of does not make a difference unless he would have excepted it had he thought of it."** The difficulty, of course, lies in determining "whether he would have excepted it" and in many instances, that question "may have no decisive answer."*** However, in the instant case, the conduct

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*Cardozo, The Nature of the Judicial Process, 15 (1921) quoting Gray, Nature and Sources of the Law, §370, p. 165

**McCallum, Legislative Intent, 75 Yale L.J. 754, 773 (1966) (emphasis in original)

***Loc. Cit.

which Congress intended to except has been explicitly articulated in the language of the statute and this provision, coupled with an examination of the circumstances compelling the statutory enactment, reveals that the Court of Appeals, rather than effectuating the Congressional intent has seriously subverted it.

1. Congressional Intent Is Revealed By the Language and Purpose of the Securities Laws.

a. The Statutory Language.

The language of the Securities Exchange Act of 1934, 15 U.S.C. §78a et seq. (Exchange Act) indicates that Congress intended to extend the protection of the United States law to foreigners injured in violation of such laws. Where a particular statutory view cannot be determined with precision, the court will look to the statute itself, to find "legislative intent."* "It

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*Citizens to Preserve Overton Park, Inc. v. Volpe, 401 U.S. 402, 412 n. 29 (1971).

is no bar to interpreting a statute as applicable that 'the question which is raised on the statute never occurred in the legislature'",* and the"absence of any legislative history in point should not outweigh the words of the statute."**

An examination of the language of the federal securities statutes indicates that Congress addressed a perceived need to regulate extraterritorial activity of Americans and foreigners which has a substantial impact upon United States commerce. Contrary to the Court of Appeals' erroneous conclusion that Congress did not consider the application of the securities laws to foreign transactions, these laws, themselves, evidence the fact

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*Eastern Airlines, Inc. v. CAB, 122 U.S. App. D.C. 375, 354 F.2d 507, 511 (1965) citing Cardozo, loc. cit.

**Souder v. Brennan, 367 F. Supp. 808, 812-813 (D.D.C. 1973).

that Congress gave such matters serious thought and, indeed, intended the securities laws to have extraterritorial effect. Thus, the subtitle of the Exchange Act is "an act to provide for the regulation of securities exchanges and all over-the-counter markets operating and in interstate and foreign commerce and through the mails to prevent inequitable and unfair practices on such exchanges and markets, and for other purposes." (emphasis supplied)

In defining "interstate commerce", Congress included instrumentalities of foreign countries as well as traditional interstate means. In Section 30(b)* Congress made clear what it would have "excepted," exempting foreign broker-dealers who engaged in securities wholly without the jurisdiction of the United States. Thus, there arises the clear inference that Congress intended that Americans and foreign persons not wholly without the jurisdiction of the United States not

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* 15 U.S.C. §78dd(b)

be exempt from the Exchange Act. Implicit in the decision to give a limited exemption is a recognition by Congress of the objective territorial principle and the fact that foreign transactions can adversely affect domestic markets. Accordingly, the statute clearly reflects the Congressional will that foreign transactions, unless exempt, be subject to the federal securities laws. In Schoenbaum, the court adopted this view stating:

> "Indeed, since Congress found it necessary to draft an exemptive provision for certain foreign transactions and gave the Commission power to make rules that would limit the exemption, the presumption must be that the Act was meant to apply to those foreign transactions not specifically exempted." 405 F.2d at 208.

Thus, the court in Schoenbaum, viewed §30b as a kind of affirmative mandate for extra-territorial application of the Exchange Act.

Additionally, in Section 30(a)* Congress delegated authority to the Securities

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*15 U.S.C. §78dd(a).

and Exchange Commission (SEC) to adopt rules to regulate the conduct of U.S. broker-dealers in transactions occurring abroad. It is significant that although the SEC, the agency entrusted with the administration of the securities laws, which has developed an unparalleled expertise in interpreting and enforcing them,* alone, was given the power to limit or define their reach to foreign transactions, the Court of Appeals arrogated to itself that Congressional grant of power.

Regretably, the court failed to utilize an elementary tool of statutory interpretation, ignoring the very language of the statute and its meaning as recognized in

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*It is further significant that although the court believed its opinion to be unprecedented and unsupported by legislative history, it did not seek advice from the SEC. Had it sought the opinion of that agency, the record in this case clearly reflects that it would have been advised that the SEC considered the antifraud provisions of the securities laws not restricted to Americans or United States residents and that such provisions attached to the challenged transaction herein.

Schoenbaum*, substituting instead its own artificial and discriminatory categories.

b. The Congressional Purpose Will Be Frustrated By Permitting the Decision of the Court of Appeals to Stand.

A court faced with the problem of statutory interpretation must examine not only the statutory language but also its aim since "[a]rguments of policy are relevant, when, for example a statute has an hiatus that must be filled or there are ambiguities in the legislative language that must be resolved."** In such case, the court should attempt "to discern and articulate the provision's purpose."*** Thus, the distillation of a statute's basic purpose

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*Schoenbaum v. Firstbrook, 405 F.2d 200 (2d Cir. 1968), reversed on other grounds, 405 F.2d 215 (2d Cir. 1968) (en banc) cert. denied sub. nom Manley v. Schoenbaum, 305 U.S. 906 (1969).

**Unexcelled Chemical Corp. v. United States, 345 U.S. 59, 64 (1953).

***Eck v. United Arab Airlines, Inc., 360 F.2d 804, 812 (2d Cir. 1965).

is necessary in any application of existing law to new conditions not dealt with in express terms.

It has been stated that "[t]he broad goal of U.S. securities laws is the promotion of securities markets whose integrity and reliability will protect investors and warrant their confidence.* The United States has long been committed to the maintenance of a domestic securities market in which all investors can participate without fear of being defrauded. As foreign investment in American markets increases, the interests of the United States in preserving the integrity of such markets from foreign wrongdoing mounts. Thus, in denying recovery to foreigners, the Court contravenes the statutory purpose, since the publicized exploitation of foreign investors by Americans in a transaction structured here adversely

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*Comment, 52 Tex. L. Rev. 983 (1974).

affected American markets. It is virtually undisputed that the shadow of disreputable activity cast by the American defendants fell upon American securities markets.* The resulting loss of foreign business was a direct and foreseeable result of defendants' activities at home and abroad in connection with the IOS offering. That it constituted a result which Congress sought to avoid cannot, petitioner submits, be fairly disputed and, accordingly, the Court had Congressional authority to administer the necessary remedy.

The decision of the Court, however, indicates a lack of awareness of the "mischief" which the securities laws were "meant to remedy" and a failure to consider the statutory purposes. The circumstances of this case present one of the very situations

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*The Court fails to distinguish between the direct "effects" caused by the participation of American principals in the securities markets in the fraud alleged and the general "effects" upon American markets resulting from the subsequent collapse of IOS, apparently lumping both together.

Congress sought to prevent by enactment of the Securities Exchange Act of 1934. Section 30(b) of that Act focused upon the single standard of "evasion." That section was intended to prevent evasion of the securities laws by devices to circumvent their application. Thus, the American broker-dealers, accountants and sellers who structured a fraudulent transaction here should not be permitted to escape liability to foreigners on the ground that they deliberately took pains to confine certain legally significant portions of their fraud to foreign shores so as to evade application of the securities laws.

It is one of the "ancient canons of interpretation that the old law, the mischief and the remedy must be considered by the judge and that the statute under consideration must be given an interpretation which will suppress the mischief and advance the remedy."*

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*Newton v. Employers Liability Assurance Corp., 107 F.2d 164, 167 (4th Cir. 1939), cert. den. 309 U.S. 673 (1940) (Parker, Circuit Judge).

It is the judge's duty "to suppress subtle inventions and evasions for the continuance of the mischief."*

This venerable maxim was endorsed by Dean Landis who observed:

> "A thorough understanding of the process underlying the statute will often give a clue as to the influence that it deserves. 'Mischiefs,' as Coke said, are often responsible for legislative action and are the key to its meaning. The consequences of the mischief may only have been appreciated by the legislature in a limited field and patent abuses alone eliminated. But thorough understanding of the statute enables one to pierce through the specific remedial measures to a concern with the causative influences that made action necessary. On the other hand, statutes may represent merely a rectification of the existing pattern of the law without striking at its deeper assumptions. Yet even rectifications, sufficiently abundant, may, like the empiric process of adjudication, spell out an attitude of more moment than the manifestations themselves, and thus bring into being a policy calling for a fuller realization."**

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* Miller v. Lykes Bros. S.S. Co., 467 F. 2d 464, 467 (5th Cir. 1972); Burstein v. United States Lines Co., 134 F. 2d 89, 93 (2d Cir. 1943).

**Statutes and the Sources of Law, 2 Harv. J. Legis. 7, 22 (1965)

It cannot be gainsaid that the federal securities laws are remedial in nature and should be given a liberal interpretation.* This Court has continually held that Congress enacted the securities laws for the purpose of preventing fraud and intended that they be construed "not technically and restrictively, but flexibly to effectuate [their] remedial purposes."** Rather than effectuate the Congressional purpose, however, the Court of Appeals' decision serves notice that American broker-dealers, accountants, issuers and sellers can defraud foreigners with impunity if they can manage to accurately "draw the line between essentially preparatory and actual fraudulent devices conducted in the U.S.,"***

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*Affiliated Ute Citizens v. United States, 406 U.S. 128 (1972); Tcherepnin v. Knight, 389 U.S. 332, 336 (1967).

**Affiliated Ute Citizens v. United States, supra, at 151; Superintendent of Insurance v. Bankers Life & Casualty Co., 404 U.S. 6, 12 (1971); SEC v. Capital Gains Research Bureau, Inc., 375 U.S. 180, 186 (1963).

***Brodsky, Corporate and Securities Litigation: The Reach of Federal Securities Laws Over Foreign Transactions, N.Y.L.J.,(May 7, 1975).

B. The Court of Appeals Opinion If Allowed to Stand Will Cause Confusion Over The Validity of Accepted Principles Regarding Jurisdiction Previously Approved By This Court.

It has been generally accepted that the principles of international law set only the outer limits of the securities laws' transnational reach, permitting a court to find that Congress intended to stop short of these limits. However, if as the Court of Appeals contends, there is an absence of evidence as to the actual Congressional intent, the court is left "with no basis except sheer speculation, for finding that Congress intended to stop short of the limits imposed by international law." In such a situation, therefore, "[t]he result is that the principles of international law function as more than mere benchmarks."*

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*Comment, The Transnational Reach of Rule 10b-5, 121 U. Pa. L. Rev. 1363, 1370. (1973). Although the Court of Appeals professed reliance upon commentary in reaching its decision, including the above cited comment, it either ignored or rejected the

The Court of Appeals, however, declined to believe that Congress intended to exercise its full power. Thus, it refused to equate the Congressional intent with the limits of international law and restricted the transnational reach of the securities laws in an opinion which "clarifies neither the source nor the scope of these limitations."* Moreover, in so doing, it misinterpreted and misapplied the basic principles of international law.

(footnote continued)

author's conclusions. The comment stated that a plaintiff who was "able to sift through the complex facts of a transnational security sale and point to elements which satisfy one or more principles" of international law would be "in a good position to satisfy his jurisdictional claim." The Court of Appeals, however, in this case as in Leasco, sought "to impose limits on the reach of Section 10(b) short of the boundaries established by international law." The comment noted "the lack of any expressed policy justification for the limits suggested by the court" in Leasco. Similarly, in the instant case, the limitation was based on no substantial policy considerations, but, rather, on a desire to destroy the class action device.

* Ibid. at 1382.

1. The Effects Doctrine Was Erroneously Applied By Misinterpretation of Precedent Laid Down by This Court.

As petitioner has discussed above, the export by Americans of the fraudulent IOS offering impaired the confidence of many foreign investors in American securities and American securities markets. As a direct result of the participation of Americans in a fraud of monumental proportions, conceived and initiated in the United States, the integrity of the American markets was impaired and the flow of capital to American business impeded. The worldwide publicity revealing Americans, identified with American securities markets, as the principal wrongdoers in a scheme to defraud foreign investors, led to a global loss of confidence in American securities markets. The impact upon such markets was undoubtedly far greater than impact previously held sufficient to justify the assertion of jurisdiction, for example, the minimal "reduction in equity" of some Americans in a Canadian corporation caused by the totally foreign transaction between foreign

entities in Schoenbaum, supra. The Court of Appeals, however, contended that such impact, even if acknowledged, would not bring the transaction within the objective territorial principle holding that domestic effects were not, as in Schoenbaum, the direct result of the wrongful conduct complained of, and, in addition, were not intended. In both contentions, the court is in error.

The intimate involvement of prominent Americans in a large international securities fraud launched from the United States necessarily adversely affects domestic markets, the very interest the securities laws were designed to protect. In discussing the "effects" issue, the court again failed to consider the purpose of the securities laws. It distinguished the result in Steele

from that herein because in the former case, there was a direct effect upon Bulova, the owner of a trademark, as a result of the defendant's infringement activities. The Court stated that nothing in the Steele opinion indicates that this Court would have found jurisdiction if all that had been proved was that the unlawful activity gave the American watchmaking industry a bad name in foreign countries. However, that distinction ignores the fact that the Lanham Trademark Act was specifically intended to protect neither industries nor markets, but specific individuals, i.e., owners of trademarks, whereas the securities laws were aimed in large part at American securities markets as a whole. Accordingly, fraudulent conduct which reflects adversely upon the integrity of such markets in foreign countries, thereby discouraging foreign investment here, is clearly not only within the ambit of international law, but also the Congressional purpose.

Further, the principles of international law do not require that to confer jurisdiction, "effects" must be intended. Judge Learned Hand's limitation on the effects doctrine followed by the Court of Appeals was superfluous, unsupported by prior law and disregarded after its articulation. Since the rule had long been established in antitrust cases that persons are presumed to intend the natural consequences of their acts, evidence of "effects" likewise evidenced the required intent. The courts after the United States v. Aluminum Co. of America* decision, have not refused to assume jurisdiction in cases of lack of intent, even where proven.**

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*Supra.

**See, e.g., United States v. National Lead Co., 63 F. Supp. 513, 518, 527 (S.D.N.Y. 1945) aff'd. 332 U.S. 319 (1947); United States v. Minnesota Mining & Mfg. Co., 92 F. Supp. 927, 958 (D. Mass. 1950); United States v. Timken Roller Bearing Co., 83 F. Supp. 284, 310 (N.D. Ohio 1949), aff'd. 341 U.S. 593 (1951); see also Thomsen v. Cayser, 243 U.S. 66, 86 (1917).

Additionally, the language of the Restatement (Second) of Foreign Relations Law of the United States, §18, cited by the Court, dealing with "effects" does not represent an accurate expression of international law and is unsupported by the "cases, authorities and the practices of states."* Indeed, the limitations contained in Section 18 were not present in the Tentative Draft and no valid justification** has been suggested for their inclusion in the final product. The Tentative Draft provided in pertinent part:

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*Metzger, The Restatement of the Foreign Relations Law of the United States: Bases and Conflicts of Jurisdiction, 41 N.Y.U. L. Rev. 7, 16 (1966).

**Prof. Metzger contends that "oil companies with international interests" mounted an attack which resulted in the change. loc. cit.

"§8. Jurisdiction to Prescribe Based on Territory: Conduct Relating to Territory

A state has jurisdiction to prescribe rules attaching legal consequences to conduct, including rules relating to property, status or other interests with respect to conduct occurring:

(a) In its territory;

(b) Partly within partly outside its territory;

(c) Entirely outside its territory, if the conduct has, or is intended to have, effects within its territory which have a reasonably close relationship to the conduct."

The Draft remains an accurate statement of the law.*

2. The Court Erred in According Jurisdictional Significance to the Distinction between Preparatory and Operative Acts, Ignoring Precedents of this Court to the Contrary.

The Court of Appeals held that the securities laws did not apply to foreign

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*Modern legislation, draft codes, projects and resolutions make "no distinction between an act and an omission to act or between an intended act or unintended result." Research in International Law: Jurisdiction With Respect to Crime, 29 Am. J. Int'l L., Special Supplement 434 (1935).

nationals resident abroad because the acts of the defendants in the United States in furtherance of the fraud, were "preparatory" in nature and the actual fraud, that is, the dissemination of the false prospectuses, primarily occurred abroad. However, petitioner submits, under the circumstances of this case, the distinction drawn is without meaning.

Petitioner alleged in the complaint that prior to their involvement in the fraud, the American defendants "knew the facts" which had caused others to decline participation in the underwriting and with knowledge of the fraudulent nature of the offering, nevertheless, determined to take part in it. Accordingly, everything done by the defendants to further the unlawful enterprise constituted illegal conduct.* The jurisdictional effect of the transaction should "not be

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*Petitioner also stated in the complaint that the existence of a conspiracy was a common question of fact.

judged by dismembering it and viewing its separate parts, but only by looking at it as a whole."*

Further, as the University of Pennsylvania comment cited by the Court of Appeals has accurately noted:

> "The requirement that the actual misrepresentations which form the basis for the 10b-5 claim be made within the United States fails to take account of the nature of transnational securities dealings. These dealings usually touch upon the territory of more than one nation, and whether a particular misrepresentation is made in one country or another is often a matter of chance. The jurisdiction of a state should not turn on such chance occurrences, for the interest of the state is identical whether or not the particular misrepresentation is made within the state. The requirement that conduct within the territory be significant, or an essential link in the transaction, is better-suited to protecting the interests of a state in regulating conduct within its borders."**

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*Continental Ore Co. v. Union Carbide & Carbon Corp., 370 U.S. 690, 699 (1962).

**121 U. Pa. L. Rev. at 1375.

C. The Court of Appeals Distorted the Significance of Nationality

The Court of Appeals determined that the scope of §10b reached Americans residing abroad, but not foreigners (in a class action) who were defrauded under identical circumstances. In reality, the court based its decision upon the American nationality of the plaintiff, a condition which it also found necessary to recovery in Leasco.* Thus, the Court subscribed to the passive personality principle, a doctrine which has been rejected by the United States.**

Not only did the court place paramount stress upon the nationality of the plaintiff, a factor generally deemed insufficient for

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*The similarity between Leasco and the instant case, is as petitioner has elsewhere suggested, the result of the influence of Judge Friendly upon the Court of Appeals in the jurisdictional area and the decisions in those cases represent his personal views.

**See Restatement (Second) of Foreign Relations Law of the United States. (1965).

jurisdiction, but it ignored the nationality of the defendants, which unlike that of the plaintiff can, in and of itself, provide a proper basis for the assertion of jurisdiction. Indeed, the nationality principle has achieved universal acceptance by members of the international community and "under existing international practice, a State is assumed to have practically unlimited legal control over its nationals."*

The United States has adopted the principle that the privileges and protection of American citizenship carry with them a duty to conform to certain standards of conduct. In particular, our government has asserted jurisdiction to punish nationals for crimes committed abroad. The courts have likewise recognized this principle in deter-

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*Research in International Law: Jurisdiction with Respect to Crime; 29 Am. J. Int'l. L. Spec. Supp., 435, 519, 520. (1935)

mining application of the securities laws. In SEC v. Gulf Intercontinental Finance Corp.*, the Court looked through "the transparent fabric" of the challenged transaction and concluded that the true issuers of the securities involved were Americans who used a Canadian corporation as "a conduit for the securities to be issued by the Florida defendants." Although the Court did not specifically base its finding of subject matter jurisdiction upon the nationality of the defendants, the facts of that case indicate that it was a determinative factor in the decision. In SEC v. United Financial Group, Inc.,** the nationality of the defendant, a Delaware corporation, was deemed a critical factor which, coupled with the fact that some Americans were allegedly defrauded and the mails and other facilities of interstate commerce of the United States were

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*223 F. Supp. 987, 995 (S.D. Fla. 1963).

**Supra.

used, provided "sufficient evidence for subject matter jurisdiction" under the American securities laws.*

In the instant case, the principal defendants are American. Defendants Drexel and Smith, Barney are United States corporations, maintaining their principal executive offices in the United States. Both are registered with the Securities and Exchange Commission as broker-dealers and are members of the National Association of Securities Dealers, Inc. These defendants

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*See also Waddell & Reed, Inc., CCH Fed. Sec. L. Rep. ¶79,049 (Securities Exchange Act Rel. No. 9790, 1972).

**See also, Finch v. Marathon Securities Corp., 316 F. Supp. 1345 (S.D.N.Y.1970), in which the Court found that the fact that six of the defendant fund's eight directors were Americans partially bridged the jurisdiction gap.

constituted two of the six principal underwriters of the primary offering and their names appeared on the cover of the main prospectus. Drexel assumed the lead position and underwrote the largest number of shares (478,000). Twenty-five additional American firms participated in the underwriting. Shares underwritten by Drexel and Smith, Barney totalled over $8,000,000, the entire American underwriting over $15,000,000. Defendant Arthur Andersen, the accounting firm which played such an important role in the preparation of the prospectus, is also an American firm. Major American law firms rendered legal advice in connection with the underwriting and in particular, the preparation of the prospectus.

Although IOS was a foreign based corporation, its image was that of an American

company.* Its president, defendant Cornfeld, its chief operating officers and many of its employees were Americans. It had formerly operated various subsidiaries in the United States, at the time of the offering was conducting a real estate enterprise in Florida, and its funds, managed by Americans, were trading heavily in American securities. Such close contact with the United States caused IOS to be viewed abroad as an American entity.

The United States has consistently treated as domestic corporations certain companies incorporated in foreign countries, but having substantial financial links with the United States and American citizens in important management positions.** Add -

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*A State has competence to exercise jurisdiction over juristic persons, including corporations, having said State's national character. Research in International Law; Jurisdiction with Respect to Crime, 29 Am. J. Int'l. L. Spec. Supp. 435, 538.

**See Foreign Asset Control Regulations.

itionally, registration with American regulatory agencies has been deemed of crucial importance. The SEC has taken the position that American broker-dealers by virtue of their registration are subject to the anti-fraud provisions of the Exchange Act. In the instant case, the SEC advised Shearman and Sterling, counsel for defendant Drexel, that the anti-fraud provisions of the Exchange Act would be applicable to the activities of a registered broker-dealer participating in an underwriting outside of the United States of a security not registered under the Securities Act of a foreign issuer to be offered and sold to foreign nationals only.*

The American nationality of the defendants was of singular importance in the

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*The SEC thus, recognized that while the United States might not wish to police the conduct of its citizens abroad in every business sphere, the Congress has specifically sought to regulate the conduct of American broker-dealers in securities transactions. Accordingly, registration with the SEC subjects the activities of such broker-dealers to regulation, wherever they may occur.

instant case, since their American identity was both a source of investor confidence in the Public Offering and disillusionment after its collapse. The exploitation of foreign nationals by American broker-dealers and accountants reflected adversely upon the United States securities markets and United States brokerage firms who were active in selling securities abroad. The IOS fraud, identified as American, resulted in a deterioration of investor confidence in American underwriters at home and abroad. "The false and misleading prospectus used in connection with the Public Offering impaired investors' confidence and trust and contributed to a steep decline in the purchase of U.S. securities by foreigners."*

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*Affidavit of Morris Mendelson, Associate Professor, Wharton School of the University of Pennsylvania, referred to in the Court of Appeals' opinion.

Thus, the fraud of Americans directly affected the integrity of American markets. It is the United States' interest in protecting the integrity of its securities markets in order to promote the free flow of capital to American business which provides a sound basis for the assertion of subject matter jurisdiction.

Accordingly, the Court of Appeals erred in overemphasizing the importance of the American nationality of the plaintiff and other American class members, while ignoring the extreme significance of the defendants' nationality, a factor which has always been accorded substantial weight in the jurisdictional scheme.*

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*In Steele v. Bulova Watch Co., supra, the court deemed significant the fact that acts of trade-mark infringement and unfair competition were consummated abroad "by a citizen and resident of the United States." at 281. In Bartholomew v. Universe Tankships, Inc., 263 F.2d 437 (2d Cir. 1959), in considering the applicability of the Jones Act to an assault on a citizen of

D. The Opinion of the Court of Appeals Written by Judge Friendly Constituted a Legislative Act Designed to Deal with the "Class Action Problem".

Judge Friendly has always stressed the legislative aspect of the judicial function, believing that upon his elevation to the bench, he "suddenly [became] a legislator, exercising power over generations yet unborn."* His strong belief that Congress has in many areas "failed to perform its legislative task"** has undoubtedly impelled him to undertake, himself, the lawmaking function so as to achieve the scheme of society which he entertains. Judge Friendly

(footnote continued)

the British West Indies, the court, "pursuant to the liberal policies of a regulatory act" looked "through the facade of foreign registration and incorporation to the American ownership" of the defendant corporation which, in turn, owned the vessel on which the assault occurred. See also, Hellenic Lines Limited v. Rhoditis, 398 U.S. 308 (1970).

*Friendly, Reactions of a Lawyer - Newly Become Judge, 71 Yale L.J. 218, 219 (1961).

has subscribed to the theory that judges should be free to impose their views of what they think desirable, quoting, with approval, the words of Learned Hand:

> "When a judge tries to find out what the government would have intended which it did not say, he puts into its mouth things which he thinks it ought to have said, and that is very close to substituting what he himself thinks right...."*

Petitioner recognizes that in some cases, particularly those in which the legislative intent cannot truly be discerned, a judge is left with a choice which permits the exercise of judicial creativity. However, petitioner submits, in this case there is a glaring contradiction between what Judge

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*Friendly, The Gap in Lawmaking - Judges Who Can't and Legislators Who Won't, 63 Colum. L. Rev. 787, 801 (1963).

**Hand, The Spirit of Liberty, 108-10 (2d Ed. 1954), cited in Friendly, The Gap in Lawmaking - Judges Who Can't and Legislators Who Won't, supra, at p. 798.

Friendly deems desirable and both the Congressional intent impelling the enactment of the securities laws and the Federal Rules of Civil Procedure. In this decision, Judge Friendly arbitrarily chose to hold that Congress did not intend to protect foreign nationals who sued as members of a class. A choice implies motives,and one can easily identify the motive which led Judge Friendly, in rendering his decision, to ignore the accepted methodology of statutory interpretation. The language of the decision itself reveals Judge Friendly's antipathy towards the class action device. The opinion initially notes with disfavor the "added complexity" inherent in "a class action on behalf of thousands of plaintiffs preponderantly citizens and residents of Canada, Australia, England, France, Germany, Switzerland and many other countries in Europe, Asia,Africa, and South America." The opinion

describes the complaint as one containing "the allegations usual when a plaintiff desires designation of his action as a class action under Fed. R. Civ. P.23(b)(3)." The Court states that Congress did not mean the United States to be used as a base for fraudulent securities schemes even when the victims are foreigners "at least in the context of suits by the SEC and by named foreign plaintiffs." However, "unhappily", says Judge Friendly, this was not a single action with named plaintiffs, but rather, a class action with many thousands of class members.

In reaching out to decide the class action issue, Judge Friendly based the Court's authority upon totally inapplicable precedent and the fact that the order appealed from had been rendered in a class action. He decided in effect, that on any interlocutory appeal in a class action, the court is not limited to the question certified, but may sua sponte

delve into the appropriateness of prior class action certification, even though such issue were not before it.* The Court gave only the most superficial consideration to the class action issue, focusing mainly on what it saw as the "tremendous burdens" imposed by a class action whose members are "predominantly

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*Class action status was previously granted herein by Judge Frankel, and the order granting such status was not appealed. A motion to review class action status was made before Judge Carter, and the motion remained undetermined by him at the time of his decision of the jurisdictional issues. Despite Judge Carter's specific statement that the class issue had not yet been resolved by him, the defendant Andersen sought to portray Judge Carter's jurisdictional decision as a class action decision in disguise and, accordingly, filed a notice of appeal thus, creating a bogus class action issue which it asserted could be heard as a matter of right. Defendant Andersen served its brief on the class action issue, and petitioner had prepared an extensive answering brief on that appeal which was rendered moot by Judge Friendly's gratuitous decision. That appeal has since been stayed.

abroad." It made no attempt to examine the scope of the manageability problem and totally ignored the benefits to be derived from the maintenance of a class action. The result was a decision against class actions per se, rather than an adjudication of jurisdictional issues. Judge Friendly articulated his subjective perception of the "good and true", seizing upon a unique opportunity to undermine class actions which he strongly believes have become "a matter that needs urgent attention". A judge who has refused to accept the class action concept, has little sympathy for those with "$50 claims" and who considers the settlement of class actions "blackmail"* has, by a feat

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* Eisen v. Carlisle & Jacquelin, 479 F.2d 1005, 1020 n. 28 (2d Cir. 1974), quoting Friendly, Federal Jurisdiction: A General View. 120 (1973).

of judicial legislation, dealt class actions a stunning blow.*

Judge Friendly's prejudice can be seen from the fact that he rendered a class action opinion without receiving the views of the appellee on the issue, a course which the appellee deems highly prejudicial, especially in light of the procedural stance of the appeal at the time the decision was rendered. Although the court had previously denied the appellant's motion to consolidate the appeal of class action issues with that of jurisdiction or to permit the appellant to submit an oversize brief so as to present class action issues, Judge Friendly seemed surprised that the appellee failed to comprehend that when the court twice said "no", it really meant "yes".

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*Not only does the elimination of foreign class members emasculate the class, but the making permanent of the stay renders settlement of a class action in which jurisdiction is challenged by a non-settling defendant impossible at any stage short of an adjudication by the United States Supreme Court.

It is clear that Judge Friendly based his decision not on the over-all dimensions of the security transaction in question, but solely upon the class action issues allegedly created by the presence of foreign members in the class, thus, distinguishing the case from prior decisions of the Second Circuit, Schoenbaum and Leasco, which did not raise "serious problems" of a class action nature. Judge Friendly indicates that a different jurisdictional result would have been found if the suit had been "by the SEC or by named foreign plaintiffs." Accordingly, by judicial legislative fiat, Judge Friendly determined in this case that foreign nationals residing abroad are, by virtue of their foreign residence, disqualified as members of a class and, accordingly, a district court lacks jurisdiction over their claims based upon violation of the securities laws, if such claims are presented by means of the class action device. Not only does such a

position find no support in either statutory law or the federal rules, but the decision is an illogical if not an irrational one. The Federal Rules of Civil Procedure cannot expand the scope of the jurisdiction of the Federal Courts beyond that conferred by Congress,nor can they contract the scope of that jurisdiction. "The issue of the power of the Court to bind foreign members of a class living abroad is difficult, unsettling, and may, in and of itself, lead to the conclusion that foreigners living abroad should not be members of the class, but that issue is unrelated to the question of the intent of Congress relating to the off-shore reach of the securities laws."*

Thus, the basic unsoundness of the decision of the Court of Appeals can be

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*Brodsky, Corporate and Securities Litigation: The Reach of Federal Securities Laws Over Foreign Transactions, N.Y.L.J.(May 7, 1975),pp. 1, 4.

explained by its underlying purpose--the frustration of class actions. The conclusions reached are grounded upon the erroneous application of international law, bolstered by faulty analysis of relevant judicial precedent and characterized by a parochial outlook, unresponsive to the problems created by the phenomenal growth in international securities trade and insensitive to the rights of individuals in a world of ever increasing transnational interaction. A decision which attempts to destroy class actions by emphasis upon citizenship as a source of rights is both dangerous and ill considered.

Judge Friendly has failed to follow the advice of Judge Learned Hand with respect to statutory interpretation rendered many years after his words quoted above.

> "[B]efore and beyond all the [judge] must purge his mind and will of those personal presuppositions and prejudices which almost inevitably invade all human judgments; he must approach his

> problems with as little preconception of what should be the outcome as it is given to men to have; in short, the prime condition of his success will be his capacity for detachment.'*

That sentiment was also expressed by one commentator who observed "that strong judges prefer to override the intent of the legislature in order to make law according to their own views," perpetrating grave sins "in the name of the intent of the Legislature." To condone "the practice of talking in terms of the intent of the legislature. . . when it is apparent that the intent is that of the judge, is to condone atavistic practices too reminiscent of the medicine man."**

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*The Spirit of Liberty, supra, 165.

**Landis, A Note on Statutory Interpretation, 43 Harv. L. Rev. 886, 890, 891 (1930).

However, "strong judges are always with us; no science of interpretation can ever hope to curb their propensities, but the effort should be to restrain their tendencies not to give them free rein in the name of scientific jurisprudence."* Nevertheless, at the least, creative judges should "hold to a 20th century economic and social philosophy and not to a long outgrown philosophy."** It is obvious that Judge Friendly would turn the clock back to the days before class actions,*** thus placing large scale injuries beyond legal redress. However, "[t]he need for group remedies is not new and has grown more acute

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*Id. 891.

**Hicks, Organization and Ethics of the Bench and Bar, 171 (1932) quoting Theodore Roosevelt.

***A long way, since as early as 1820, Justice Story approved the representative action. West v. Randall, 29 Fed. Case. 718, 720-22 (No. 17,424) (C.C.D. R.I. 1820).

as commercial and social transactions have increased in complexity and dispersion ."* Thus, "[w]hat life needs, the law must reckon with."**Class action litigation has become a valuable part of the American judicial process and it should not, plaintiff submits, be vitiated in the name of a fictitious Congressional intent.

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*Note, Federal Class Actions; A Suggested Revision of Rule 23, 46 Colum. L. Rev. 818 (1946).

**Brown, Electronic Brains and the Legal Mind: Computing the Data Computer's Collision with Law, 71 Yale L.J. 239, 254 (1961).

CONCLUSION

The issues herein presented are of increasing importance, as the securities markets of the world grow more interrelated. The decision admittedly represents not the views of Congress, but those of one appellate panel. That decision, by permitting the evasion of liability in an international securities transaction by the strategic placement of fraudulent actions, encourages the exploitation of foreign investors and the flouting of American law. It is, therefore, important that this Court reaffirm the principles behind the federal securities laws by upholding

subject matter jurisdiction with respect to the claims of the entire class. Accordingly, the petition for writ of certiorari should be granted.

Respectfully submitted,

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